

**Letter of Findings: 04-20181674
Gross Retail and Use Tax
For the Years 2012 through 2015**

NOTICE: IC § 6-8.1-3-3.5 and IC § 4-22-7-7 require the publication of this document in the Indiana Register. This document provides the general public with information about the Department's official position concerning a specific set of facts and issues. This document is effective on its date of publication and remains in effect until the date it is superseded or deleted by the publication of another document in the Indiana Register. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Letter of Findings.

HOLDING

The Department agreed that Audio Equipment Company met its burden of establishing that the Department's assessment of additional sales/use tax was overstated; Audio Equipment Company provided documentation verifying that it was assessed for otherwise exempt transactions such as labor charges and transactions for which Indiana sales/use tax had previously been paid.

ISSUES

I. Gross Retail and Use Tax - Out-of-State Transactions.

Authority: IC § 6-2.5-2-1(a); IC § 6-2.5-2-1(b); IC § 6-2.5-3-1(a); IC § 6-2.5-3-2(a); IC § 6-8.1-5-1(c); *Dept. of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289 (Ind. Tax Ct. 2007); *Wendt LLP v. Indiana Dep't of State Revenue*, 977 N.E.2d 480 (Ind. Tax Ct. 2012); *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138 (Ind. Tax Ct. 2010); *Rhoads v. Ind. Dep't of State Revenue*, 774 N.E.2d 1044 (Ind. Tax Ct. 2002).

Taxpayer argues it was not responsible for paying sales tax or self-assessing use tax on the purchase of items which were used by or at one of its out-of-state facilities.

II. Gross Retail and Use Tax - Intercompany Transactions.

Authority: IC § 6-2.5-2-1(a); IC § 6-2.5-3-2(a); IC § 6-8.1-5-1(c).

Taxpayer states it was not responsible for paying sales tax or self-assessing use tax on expenses related to "intercompany" or shared service expenses.

III. Gross Retail and Use Tax - Exempt Services.

Authority: [45 IAC 2.2-4-2](#); [45 IAC 2.2-4-2](#)(a); IC § 6-8.1-5-1(c).

Taxpayer argues that the Department's audit erroneously assessed sales/use tax on Taxpayer's purchase of exempt services.

IV. Gross Retail and Use Tax - Calculation Errors / Tax Paid.

Authority: IC § 6-8.1-5-1(c).

Taxpayer claims that the Department's audit erred in assessing sales/use tax on transactions for which tax had been paid.

V. Gross Retail and Use Tax - Research and Development Property.

Authority: IC § 6-2.5-3-1(a); IC § 6-2.5-3-2(a); IC § 6-2.5-5-40; IC § 6-2.5-5-40(a); IC § 6-2.5-5-40(b); IC § 6-2.5-5-40(d); IC § 6-2.5-5-40(e)(10); IC § 6-8.1-5-1(c); *Conklin v. Town of Cambridge City*, 58 Ind. 130 (1877); *Mynsberge v. Dep't of State Revenue*, 716 N.E.2d 629 (Ind. Tax Ct. 1999); *Tri-States Double Cola Bottling Co. v. Dep't of State Revenue*, 706 N.E.2d 282 (Ind. Tax Ct. 1999); *Rhoads v. Ind. Dep't of State Revenue*, 774 N.E.2d

Taxpayer argues it was not required to pay sales or use tax on the purchase of certain equipment on the ground that the equipment qualifies for the research and development sales tax exemption.

STATEMENT OF FACTS

Taxpayer is an Indiana company which manufactures, sells, and installs audio equipment. Taxpayer has a business relationship with out-of-state affiliates and conducts business activities both within and outside the United States. The Indiana Department of Revenue ("Department") conducted an audit review of Taxpayer's 2012 through 2015 business records, sales and purchase transactions, and tax returns.

Based on the substantial number of 2012 through 2015 Taxpayer's records, the Department decided to prepare a "statistical sampling" of those records. Taxpayer agreed to the sampling methodology and signed form AD-10A ("Agreement for Projecting Audit Results") to that effect. That sample was used to calculate any additional tax liability.

The Department's audit resulted in assessments of additional sales/use tax. According to the Department's audit report, the assessments resulted from: (1) Taxpayer's failure to obtain "properly executed exemption certificates" from certain of its customers; (2) Taxpayer purchased taxable "computer hardware, canned software, and accessories" without paying sales tax; (3) Taxpayer purchased various taxable "promotional items" without paying tax; (4) Taxpayer purchased taxable "meals, banquets, and food and beverage" without paying sales tax; and (5) Taxpayer rented furniture without paying sales tax. In addition, the Department found that Taxpayer purchased various capital items such as light fixtures and other items without paying sales or use tax.

Taxpayer disagreed with the assessment and submitted a protest to that effect. An administrative hearing was conducted during which Taxpayer's representatives explained the basis for the protest. This Letter of Findings results.

I. Gross Retail and Use Tax - Out-of-State Transactions.

DISCUSSION

Taxpayer states that it was assessed tax on transactions which occurred entirely outside Indiana. For example, Taxpayer explained that it was incorrectly assessed tax on transactions in which the buyer - one of its affiliates - was located outside Indiana and the seller was also located outside Indiana. According to Taxpayer, although it has a business relationship with the affiliate/buyer, neither it nor the named buyer are individually subject to Indiana's sale or use tax and that these transactions should be removed from the audit's "sample" on which the Department determined the challenged assessment.

As a threshold issue, it is the Taxpayer's responsibility to establish that the existing tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463, 466 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007). Thus, a taxpayer is required to provide documentation explaining and supporting its challenge that the Department's position is wrong. Poorly developed and non-cogent arguments are subject to waiver. *Scopelite v. Indiana Dep't of Local Gov't Fin.*, 939 N.E.2d 1138, 1145 (Ind. Tax Ct. 2010); *Wendt LLP v. Indiana Dep't of State Revenue*, 977 N.E.2d 480, 486 n.9 (Ind. Tax Ct. 2012). Further, "[W]hen [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] defer to the agency's reasonable interpretation of [the] statute even over an equally reasonable interpretation by another party.'" *Dept. of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579, 583 (Ind. 2014). Thus, interpretations of Indiana tax law contained within this decision, as well as the preceding audit decision, are entitled to deference.

Indiana imposes an excise tax called "the state gross retail tax" (or "sales tax") on retail transactions made in Indiana. IC § 6-2.5-2-1(a). A person who acquires property in a retail transaction (a "retail purchaser") is liable for the tax on the transaction. IC § 6-2.5-2-1(b).

Indiana also imposes a complementary excise tax called "the use tax" on "the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC § 6-2.5-3-2(a). Use means the "exercise

of any right or power of ownership over tangible personal property." IC § 6-2.5-3-1(a).

In effect and practice, the use tax is functionally equivalent to the sales tax. See *Rhoads v. Ind. Dep't of State Revenue*, 774 N.E.2d 1044, 1047 (Ind. Tax Ct. 2002).

As Taxpayer correctly notes, Indiana's sales tax is imposed on retail transactions which are "made in Indiana," IC § 6-2.5-2-1(a), while the complementary use tax is imposed on property used or consumed in Indiana regardless of where the property was originally purchased. IC § 6-2.5-3-2(a).

As to the following payments, Taxpayer has met its burden under IC § 6-8.1-5-1(c) of establishing that the transactions should not have been included in the audit sample.

- Invoice number 337E4, dated February 6, 2014, JW Marriott;
- An unnumbered invoice dated November 15, 2012, Hyatt Regency;
- Invoice number HBT2015, dated January 27, 2015, Beverly Hilton;
- Invoice number 60039, dated October 4, 2015, Palais Frankfurt, Germany;
- Invoice number 50518, dated July 4, 2015, Kofler & Kompanie, GMBH;
- Invoice number 60050, dated July 5, 2015, Palais Frankfurt, Germany;
- Invoice number 101656, dated October 31, 2012, National Academy of Recording Arts & Sciences;
- Invoice number 316418, dated November 30, 2014, Harman/Becker Automotive;
- Invoice number ODL1283, dated June 23, 2013, Oxford Digital;
- Invoice number 92581751, dated August 19, 2015, CSA Group;
- Invoice number LR950090, dated November 30, 2013, DSV Solutions A/S;
- Invoice number IN120787, dated January 31, 2012, MSI Meeting Services, Inc.;
- Invoice number 18641-561-12-9921, dated December 20, 2011, infoComm International;
- Invoice number 3801, dated January 30, 2012, MBoxDesign;
- Invoice number 3779, dated January 26, 2012, MBoxDesign;
- Invoice number 3789, dated January 26, 2012, MBoxDesign;
- Invoice number 10292858, dated July 15, 2015, PTC Inc.;
- Invoice number 29632, dated January 24, 2013, Up Beat Daily;
- Invoice number 7442, dated May 23, 2012, Renaissance Hotel;
- Invoice number 3371121115, dated March 9, 2012, Newport Beach Marriott Hotel.

Taxpayer has met its burden under IC § 6-8.1-5-1(c) of establishing that assessment of tax on these transactions was "wrong."

FINDING

As to the transactions designated in Part I above, Taxpayer's protest is sustained.

II. Gross Retail and Use Tax - Intercompany Transactions.

DISCUSSION

Taxpayer maintains that it was incorrectly assessed sales/use tax on "intercompany transactions" in which one of its out-of-state affiliates entered into a sale of taxable goods to another of Taxpayer's out-of-state affiliates. According to Taxpayer, "This very significant piece of the audit accounts for the majority of the error percentage."

As noted above, Indiana's sales and use tax generally is imposed on sales of tangible personal property which occur in Indiana or the acquisition of tangible personal property which is used, stored, or consumed in this state. IC § 6-2.5-2-1(a); IC § 6-2.5-3-2(a).

- Invoice 9101A, dated December 21, 2013, for \$554,268 which lists intercompany charges for a series of expenses none of which are related to the purchase or use of "tangible personal property."

Taxpayer has met its burden under IC § 6-8.1-5-1(c) of establishing that assessment of tax on this transaction was "wrong."

FINDING

As to the transaction designated in Part II above, Taxpayer's protest is sustained.

III. Gross Retail and Use Tax - Exempt Services.

DISCUSSION

Taxpayer argues that it was incorrectly assessed sales/use tax on its purchase of exempt services.

Taxpayer relies on [45 IAC 2.2-4-2](#) as authority for its position that these purchases are exempt from sales/use tax.

[45 IAC 2.2-4-2](#) provides as follows:

- (a) Professional services, personal services, and services in respect to property not owned by the person rendering such services are not "transactions of a retail merchant constituting selling at retail", and are not subject to gross retail tax. Where, in conjunction with rendering professional services, personal services, or other services, the serviceman also transfers tangible personal property for a consideration, this will constitute a transaction of a retail merchant constituting selling at retail unless:
 - (1) The serviceman is in an occupation which primarily furnishes and sells services, as distinguished from tangible personal property;
 - (2) The tangible personal property purchased is used or consumed as a necessary incident to the service;
 - (3) The price charged for tangible personal property is inconsequential (not to exceed 10[percent]) compared with the service charge; and
 - (4) The serviceman pays gross retail tax or use tax upon the tangible personal property at the time of acquisition.
- (b) Services performed or work done in respect to property and performed prior to delivery to be sold by a retail merchant must however, be included in taxable gross receipts of the retail merchant.
- (c) Persons engaging in repair services are servicemen with respect to the services which they render and retail merchants at retail with respect to repair or replacement parts sold.
- (d) A serviceman occupationally engaged in rendering professional, personal or other services will be presumed to be a retail merchant selling at retail with respect to any tangible personal property sold by him, whether or not the tangible personal property is sold in the course of rendering such services. If, however, the transaction satisfies the four (4) requirements set forth in 6-2.5-4-1(c)(010), paragraph (1) [subsection (a) of this section], the gross retail tax shall not apply to such transaction.

The regulation on which Taxpayer depends, [45 IAC 2.2-4-2](#), contains a provision exempting the purchase of services from sales tax. [45 IAC 2.2-4-2\(a\)](#) states that, "Professional services, personal services, and services in respect to property not owned by the person rendering such services are not transactions of a retail merchant constituting selling at retail, and are not subject to gross retail tax." However, "Where, in conjunction with rendering professional services . . . the serviceman also transfers tangible personal property for a consideration, this will constitute a transaction of a retail merchant constituting selling at retail . . ." *Id.*

As to the following payments, Taxpayer has provided documentation which is sufficient to meet its burden of establishing that the transactions are one for which Taxpayer was purchasing and paying for exempt services.

- Invoice number 26293523, dated October 27, 2013, Manpower;
- Unnumbered Invoice, dated January 19, 2012, DLS Electronic Systems, Inc.;
- Invoice number 1970, dated November 17, 2015, Definition Branding & Marketing;
- Invoice number 2015 08 19, dated August 19, 2015, Harman Professional;
- Invoice 2015 08 19, dated August 19, 2015, Harman Professional;
- Invoice 2015 08 19, dated August 19, 2015, Harman Professional;
- Invoice 2015 08 19, dated August 19, 2015, Harman Professional;
- Invoice number 12275305, dated October 20, 2013, Spherion;
- Invoice number 4910, dated January 2, 2013, Marketing Information Services, Inc.;
- Invoice number 4988, dated July 17 2013, Marketing Information Services, Inc.

Taxpayer has met its burden under IC § 6-8.1-5-1(c) of establishing that assessment of tax on these transactions was "wrong."

FINDING

As to the transactions designated in Part III above, Taxpayer's protest is sustained.

IV. Gross Retail and Use Tax - Calculation Errors / Tax Paid.**DISCUSSION**

Taxpayer states that the Department's audit sample contains calculation errors including instances in which the Department assessed tax on transactions for which the sales had already been paid. As explained by Taxpayer, "The auditor includes sales where sales tax was included on the invoice." As to the following transactions, Taxpayer has met its statutory burden under IC § 6-8.1-5-1(c) of establishing that the transaction should not have been included in the audit sample.

- Invoice account number 048-737-529-0-3, disconnect notice dated December 4, 2013, Indiana Michigan Power;
- Invoice number 0003974-IN, dated December 18, 2012, Essenhaus, Inc.
- Unnumbered invoice, dated April 19, 2012, Nelson's;
- Unnumbered invoice, dated March 5, 2012, Newport Beach Marriott Hotel;
- Unnumbered invoice, dated March 6, 2012, Newport Beach Marriott Hotel;
- Unnumbered invoice, dated March 6, 2012, Newport Beach Marriott Hotel;
- Unnumbered invoice, dated March 6, 2012, Newport Beach Marriott Hotel.

Taxpayer has met its burden under IC § 6-8.1-5-1(c) of establishing that assessment of tax on these transactions was "wrong."

FINDING

As to the transactions designated in Part IV above, Taxpayer's protest is sustained.

V. Gross Retail and Use Tax - Research and Development Property.**DISCUSSION**

Taxpayer purchased items of tangible personal property from Application Solutions in 2015. The property - consisting of various items of audio equipment - was purchased outside the state and delivered to Taxpayer's Indiana location. The Department's audit assessed use tax on the transactions which Taxpayer here challenges on the ground that the items consist of exempt research and development equipment.

As noted in Part I, Indiana imposes a complementary excise tax called "the use tax" on "the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." IC § 6-2.5-3-2(a). Use means the "exercise of any right or power of ownership over tangible personal property." IC § 6-2.5-3-1(a).

In effect and practice, the use tax is functionally equivalent to the sales tax. See *Rhoads v. Ind. Dep't of State Revenue*, 774 N.E.2d 1044, 1047 (Ind. Tax Ct. 2002).

However, Indiana law, IC § 6-2.5-5-40 (effective January 1, 2016) explains that a taxpayer is entitled to purchase certain items of tangible personal property without paying the retail tax when the property consists of "research and development equipment" and is "devoted directly to experimental or laboratory research." IC § 6-2.5-5-40(b). IC § 6-2.5-40(g) renders the provision effectively retroactive to transactions "occurring after June 30, 2015[.]"

IC § 6-2.5-5-40(d) was added in 2015 to exclude items which are "incidental" to otherwise qualified research and development projects. In part, the statutory clarification states:

[Research and Development] does not include activities incidental to experimental or laboratory research and development [and] . . . any other function that is incidental to experimental or laboratory research and development.

Taxpayer explains that its purchase of the equipment is exempt because the transaction fell within the exemption. The Department notes however that IC § 6-2.5-5-40, like all tax exemption provisions, is strictly construed against exemption from the tax. *Tri-States Double Cola Bottling Co. v. Dep't of State Revenue*, 706 N.E.2d 282, 283 (Ind. Tax Ct. 1999); *Mynsberge v. Dep't of State Revenue*, 716 N.E.2d 629, 636 (Ind. Tax Ct. 1999). Indiana law has long held that "where [] an exemption is claimed, the party claiming the same must show a case, by sufficient

evidence, which is clearly within the exact letter of the law." *Indiana Dep't of State Revenue, Sales Tax Division v. RCA Corp.*, 310 N.E.2d 96, 101 (Ind. Ct. App. 1974). 1 (citing *Conklin v. Town of Cambridge City*, 58 Ind. 130, 133 (1877)).

In this instance, Taxpayer purchased various items of equipment which may well be directly used in in [sic] the "design, refinement and testing of . . . new or improved commercial products . . ." IC § 6-2.5-5-40(a). In contrast, the items could also be used in activities entirely "incidental to experimental laboratory research and development." IC § 6-2.5-5-40(e)(10). From the information provided - which consists solely of the original invoice - it is not possible to agree with Taxpayer that it has met its statutory burden under IC § 6-8.1-5-1(c) of establishing that the audit's decision to classify as these purchase as "taxable" is itself "wrong." Taxpayer has not established that the 2015 purchases from Application Services were exempt.

In short, Taxpayer's original invoice alone is not sufficient to establish that the items purchased from Application Services in 2015 were exempt from Indiana sales and use tax under IC § 6-2.5-5-40.

FINDING

Taxpayer's protest is respectfully denied.

SUMMARY

As set out in the Letter of Findings and except for the claim that its equipment qualified for the research and development exemption, the Department incorrectly assessed sales/use tax on specific transactions which should be removed from the audit sample relied upon to calculate Taxpayer's sales/use tax assessment.

November 7, 2018

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